DRAFT

STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date:	**03/10/14**	Bill No:	**Assembly Bill 2114**
Tax Program:	**Property Heavy Equipment**	Author:	**Pan**
Sponsor:	**Author**	Code Section:	**RTC 97.38 and 5500, et seq.**
		Effective Date:	**01/01/15**

BILL SUMMARY

In lieu of business personal property tax, this bill imposes a 0.75% tax on a rentee of qualified heavy equipment to be collected by a qualified renter.

ANALYSIS

CURRENT LAW

Property Tax. Under existing law,[1] all property is taxable unless specifically exempt under the Constitution or Revenue and Taxation Code. The county assessor determines taxability each year, generally on the January 1 lien date.

Personal property used in a trade or business is generally taxable. Property owners must file an annual business property statement with the county assessor to report the cost of the property.[2] The assessor values the personal property each lien date at its current fair market value. Generally, the assessor determines the current fair market value based on the property's acquisition cost with adjustments for inflation and depreciation.

The personal property tax rate is the same as the rate levied on real property. That rate is 1%, plus any local voter-approved indebtedness.

Regarding personal property taxation, California's Constitution[3] authorizes the Legislature by a 2/3 vote to classify personal property for different taxation or for exemption.

The law provides no specific tax exemption for heavy equipment leases or rentals (rentals). However, a personal property business inventory exemption[4] is available. Personal property intended for rent in the regular course of business that is *not* rented on the January 1 lien date is exempt from taxation for the upcoming fiscal year (July 1 to June 30). That property is regarded as business inventory on that particular day, even if the property is rented in the regular course of business for the other 364 days of the year.

Revenue Distribution. Generally, personal property tax revenues are allocated according to the property's "situs" (location) and accrue only to those taxing jurisdictions in the tax rate area where the property is located. Under a Board of Equalization (BOE) rule,[5] property rented on a daily, weekly, or other short-term basis (six months or less)

[1] Part 1 (commencing with Section 50) of Division 1 of the Revenue and Taxation Code (RTC).
[2] RTC Section 441.
[3] California Constitution Article XIII, Section 2.
[4] RTC Section 219.
[5] Property Tax Rule 204.

has situs where the property's owner (the renter) normally keeps the property. Temporary absences from that location do not change the property's situs. For property rented for an extended, but unspecified, period or more than a 6-month term, the assessor determines the property's situs based on the rentee's use. For typical equipment rentals, generally the equipment's owner is the assessee subject to the tax.[6] However, the facts specific to each case determine the assessee.

PROPOSED LAW

This bill imposes[7] a 0.75% tax on a rentee, as defined, for a qualified heavy equipment rental, as defined. The proposed tax is in lieu of any property tax on this equipment. The bill requires the heavy equipment's qualified renter to collect the tax on the rental price, and requires the BOE to administer the tax.

A qualified heavy equipment renter must separately state the tax imposed on any contract, receipt, invoice, or other similar document given to the qualified rentee at the rental time.

The bill specifies that a business' qualified heavy equipment that is not for rent shall remain subject to any applicable property taxes.

Administration. This bill requires the BOE to administer and collect the tax pursuant to the Fee Collection Procedures Law (FCPL).[8] For purposes of the tax, the bill clarifies that under the FCPL:

- "Fee" includes the tax; and
- "Feepayer" includes a person that is liable for payment of the tax.

The FCPL generally provides for the BOE's administration of fee programs. Among other things, the FCPL provides for collection, reporting, return, refund, and appeals procedures, as well as the BOE's authority to adopt regulations related to the FCPL's administration and enforcement. The bill also specifically authorizes the BOE to prescribe and adopt tax administration and enforcement regulations.

Registration, Reporting, and Payment. The bill requires every qualified renter to register with the BOE using a BOE-prescribed application, as described.

The tax imposed is due and payable to the BOE quarterly on or before the last day of the month following each calendar quarter. Qualified renters must file a return using electronic media on or before the last day of the month following each quarterly period.

Both the application and the return may be authenticated in a form or pursuant to a method as the BOE may prescribe.

Disposition of Proceeds. This bill requires all revenues, interest, penalties, and other amounts collected, less refunds and the BOE's administrative costs, to be deposited in the state's General Fund.

Definitions. This bill defines several key terms, as follows:

- "**Qualified rentee**" means a rentee that rents qualified heavy equipment from a qualified renter.

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6 RTC Section 405.
7 RTC Section 97.38 and Part 11 (commencing with Section 5500)
8 RTC Part 30 (commencing with Section 55001).

- "**Qualified renter**" means a renter (1) whose principal business is the short-term rental of qualified heavy equipment, and (2) is engaged in a line of business described in the 2012 edition of the North American Industry Classification System (NAICS) Code 532412, as specified.
- "**Rental price**" means the total charge for renting the equipment, excluding other charges as specified.
- "**Renting**" or "**rent**" means a rental for a period of less than 365 days or for an undefined period.
- "**Qualified heavy equipment**" means construction, earthmoving, or industrial equipment that is mobile, including, but not limited to the following*:*

  (1) A self-propelled vehicle that is not designed to be driven on the highway.

  (2) Industrial electrical generation equipment.

  (3) Industrial lift equipment.

  (4) Industrial material equipment.

  (5) Equipment used in shoring, shielding, and ground trenching.
- "**Local entity**" means a city, county, and special district.

LEGISLATIVE HISTORY

In 2013, Assembly Bill 1055 (Pan) proposed a similar tax, as did a 2012 bill, Assembly Bill 1941 (Ma). The Assembly Revenue and Taxation Committee held both bills.

COMMENTS

1. **Sponsor and Purpose.** As the sponsor, the author's office notes that some heavy equipment rental companies contend that subjecting heavy equipment to personal property taxation results in both unfairness and administrative inconsistencies. Specifically, rental companies with multiple locations in the state are subjected to numerous audits each year in different jurisdictions. In addition, they state that different county assessors use different methods for valuing mobile construction equipment. This measure is intended to address that unfairness and inconsistency.
2. **In lieu of personal property taxation.** Heavy equipment, as described in the bill, is regarded as personal property upon which property tax is assessed. As personal property, the Legislature is constitutionally authorized to provide for a differential tax, such as the tax proposed in this bill. A similar differential tax on personal property applies to vehicles. In 1936, the creation of the Vehicle License Fee removed vehicles from local county assessment and subjected them to a Department of Motor Vehicles-administered vehicle license fee. The fee is in lieu of the property tax under current law.[9] The 1936 change stemmed from the inability to effectively assess and collect taxes on vehicles via the property tax. Noted problems at the time included significant tax evasion, relatively high administrative costs, and little statewide uniformity in values assigned to similar vehicles.
3. **Implementation Costs.** Although the bill authorizes reimbursement of the BOE's costs through the revenues collected, in order for the BOE to receive reimbursement for the necessary implementation costs up front, it is recommended that the bill authorize the Director of Finance to authorize a loan from the General Fund to the BOE to meet cash needs.

9 RTC Section 10758.

4. **Who is a "qualified renter?"** The bill defines a qualified renter as one whose principal business is the short-term rental of qualified heavy equipment and who is engaged in a business described in NAICS Industry Code 532412. This code describes establishments that are primarily engaged in a line of business renting or leasing heavy equipment without operators that may be used for construction, mining, or forestry. This includes bulldozers, earthmoving equipment, oil well or other well-drilling machinery and equipment, logging, or cranes.

5. **What about bad debts?** The bill is clear that the rentee's liability for the tax is not extinguished until the tax is paid to the renter. However, the author may also wish to consider amending the bill to relieve a qualified renter from the tax liability for accounts found worthless and charged-off for income tax purposes.

6. **Technical issue.** The bill defines the term "local entity"; however, the term is not used in the proposed language.

COST ESTIMATE

BOE administrative costs related to this bill are likely to be significant. These costs include taxpayer identification, notification, and registration; regulation development; manual and publication revisions; tax return design; computer programming; return, payment, and refund claim processing; audit and collection tasks; staff training; and public inquiry responses.

A detailed cost estimate is pending.

REVENUE ESTIMATE

BACKGROUND, METHODOLOGY, AND ASSUMPTIONS

Based on 2007 *Census* data and the 2012 *Service Annual Survey* (SAS), we estimated that for establishments primarily engaged in NAICS Code 532412 (Construction, Mining, and Forestry Machinery and Equipment Rental and Leasing), California rental receipts were $2 billion in 2012. Using an industry forecast, estimated receipts for calendar year 2015 would amount to $2.23 billion. It should be noted that we do not have data regarding the property tax revenues heavy equipment renters currently pay.

REVENUE SUMMARY

The proposed 0.75% tax rate on $2.23 billion in receipts would yield estimated gross revenues of $16.7 million (0.75% × $2.23 billion = $16.7 million) annually.

Qualifying Remarks. As stated previously, we do not have data regarding the property tax revenues heavy equipment renters currently pay. In a 2013 analysis, the Legislative Analyst's Office also indicated the same but did suggest that property tax on rental equipment likely generates $20 million to $25 million annually for local governments. Also, this revenue estimate does not account for any changes in economic activity that may or may not result from enactment of the proposed law.

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